

ESTIMATED SURPLUS/(DEFICIT)

The Mayor's 2004-2005 Proposed Budget assumes no General Fund surplus or deficit for the current year (2003-2004). However, based on its most recent analysis of various appropriations and revenues, the Budget Department currently projects a deficit of \$311,400, which consists of a net surplus in revenues of \$50.2 million and a net deficit in appropriations of \$50.5 million. Estimates of revenue collections used to calculate the surplus/deficit appear reasonable.

Those agencies expected to generate a surplus or deficit greater than \$0.5 million are highlighted in the table below. Agencies expected to have a surplus or deficit less than \$0.5 million have been netted together and are shown as Other Agencies (Net).

<u>Surplus (Deficit) Identified By General Fund Department or Item</u>	<u>Revenue Surplus/(Deficit)</u>	<u>Appropriations Surplus/(Deficit)</u>	<u>Net Surplus/(Deficit)</u>
City Council	\$ (700)	\$ 1,363,000	\$ 1,362,300
Civic Center	(1,418,000)	484,000	(934,000)
Department of Public Works	(2,000,000)	(2,393,000)	(4,393,000)
Election Commission	800	855,200	856,000
Environmental Affairs	(2,505,000)	211,000	(2,294,000)
Finance	(2,427,000)	4,626,000	2,199,000
Fire	2,476,000	(1,392,000)	1,084,000
Health	(1,441,000)	3,050,000	1,609,000
Information & Technological Services	(700,000)	2,986,000	2,286,000
Law	300,000	1,312,000	1,612,000
Planning & Development	832,000	126,000	958,000
Police	(1,425,000)	(10,962,000)	(12,387,000)
Recreation	(401,000)	(548,000)	(949,000)
36 th District Court	1,450,000	(105,000)	1,345,000
Zoological Institute	(1,347,000)	(118,000)	(1,465,000)
Other Agencies (Net)	(2,037,700)	4,376,000	2,338,300
Non-Departmental	(8,300,000)	11,141,000	2,841,000
Fringes	-	3,620,000	3,620,000
Sub total	\$ (18,943,600)	\$ 18,632,200	\$ (311,400)
Prior Year Deficit	69,100,000	(69,100,000)	-
Total Projected General Fund Surplus/(Deficit)	\$ 50,156,400	\$ (50,467,800)	\$ (311,400)

Vacancies, the hiring freeze, overtime restrictions and general management of accounts resulted in appropriation surpluses, the Budget Department reported. In addition, the Budget Department attributed surpluses to Risk Management, Undistributed Fringes and Hospitalization

The revenue deficit stemmed from cuts in State Revenue Sharing, revenue shortfalls in the departments including civil infractions, Construction Inspection and Street Fund,

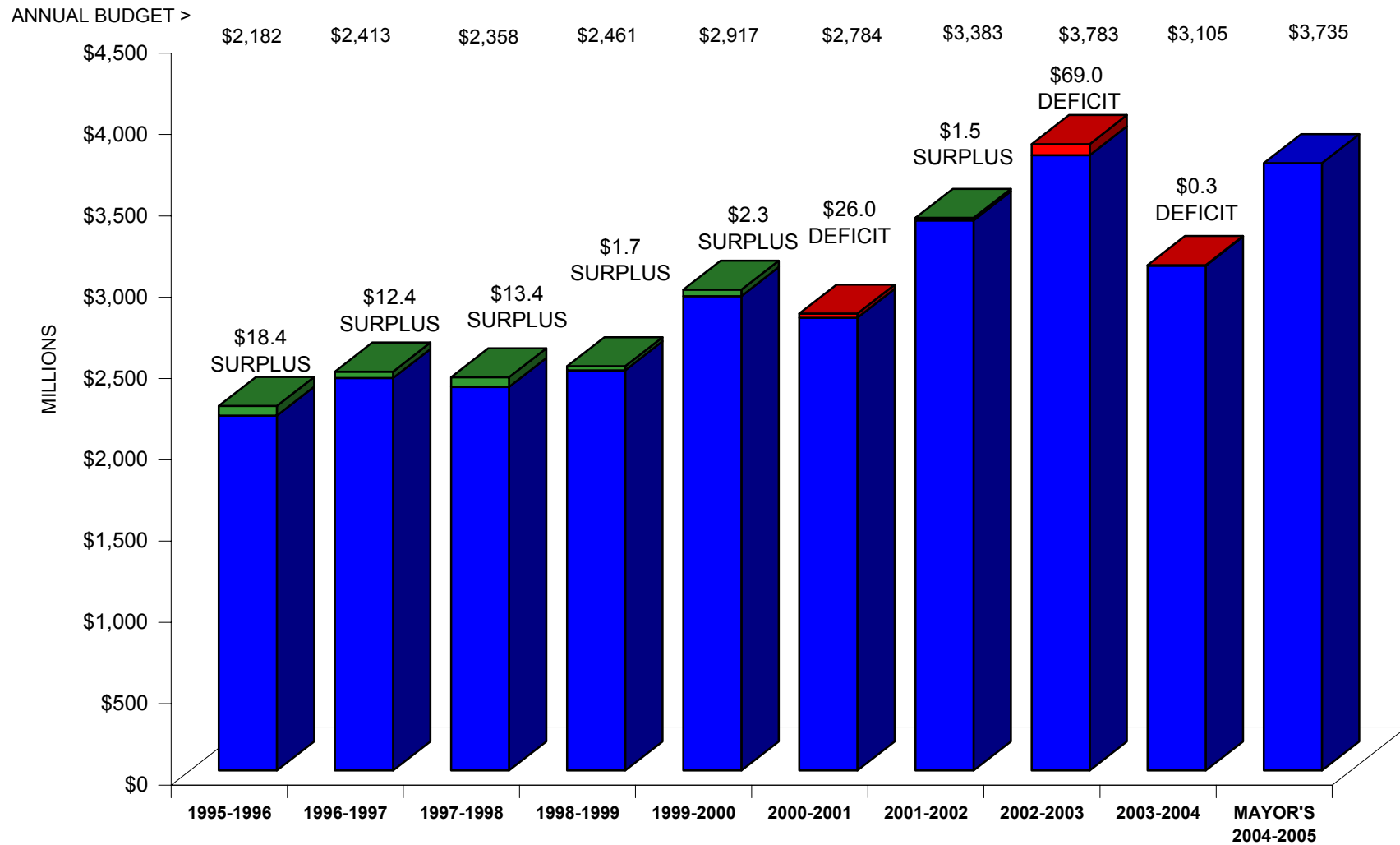
Cultural Reimbursement and Rental of Public Buildings. These deficits are offset by an expected increase in Municipal Income Tax and in Wagering Tax, as well as by the proceeds of an agreement with Wayne County to collect the City's delinquent property taxes. The agreement with Wayne County boosted the estimate of 2003-2004 Prior Year Property Tax Revenues by over \$15.0 million.

The Budget Department's April 2004 estimate of the 2003-2004 deficit is based on the best available information and on various assumptions and projections, and is subject to change.

COMPARATIVE TOTAL FISCAL YEAR BUDGETS

(INCLUDING ACTUAL SURPLUSES and DEFICITS)

(In Millions)



BUDGET STABILIZATION RESERVE FUND

Detroit's Budget Stabilization Reserve Fund, a "rainy day fund," was established by City ordinance in 1979. City Ordinances 324-H and 341-H provide that one-half of a General Fund surplus for a fiscal year will be included as revenue in the following year's budget and the other one-half of the surplus will be transferred to the Budget Stabilization Reserve Fund. The Budget Stabilization Reserve Fund, accounted for as a reserved portion of the General Fund's fund balance, was established to cover future General Fund deficits, provide funds to restore employees laid off during prior fiscal years, and to cover expenses arising from natural disasters.

The Budget Stabilization Reserve Fund's current balance is approximately \$8.5 million. The following table shows the composition of the Budget Stabilization Reserve Fund balance:

<u>Fiscal Year</u>	<u>In Millions</u>			<u>Fund Balance on June 30</u>
	<u>Surplus/ (Deficit)</u>	<u>Deposits</u>	<u>Withdrawals</u>	
1994-1995	\$20.0			\$ 0.0
1995-1996	18.4	\$10.0		10.0
1996-1997	12.4	9.2		19.2
1997-1998	13.4	6.2		25.4
1998-1999	1.6	6.7		32.1
1999-2000	2.3	0.8		32.9
2000-2001	(26.4)	1.2		34.1
2001-2002	1.6		\$(26.4)	7.7
2002-2003	(69.1)	0.8		8.5
2003-2004	0.0 (A)		(8.5)	0.0 (A)

(A) Projection

The Mayor's 2004-2005 Proposed Budget includes a withdrawal of \$8.5 million during the fiscal year 2003-2004 to partially offset the \$69.1 million deficit the City experienced in fiscal year 2002-2003. As a result, the Budget Stabilization Reserve Fund balance is projected to have a zero balance as of June 30, 2004. The Mayor's Proposed Budget projects that the City will not have a surplus or deficit for fiscal year 2003-2004.

RISK MANAGEMENT FUND

The Risk Management Fund is a self-insurance fund established by City Ordinance (Ord. No. 16-95) in 1995 to cover liability to third parties for any loss or damage arising out of negligence, tort, contract or otherwise accruing, payable by the City from and after July 1, 1994.

The City may be liable under Workers' Compensation or Disability Benefits Law, or under any similar laws, or for damage to property or personal injury, in accordance with applicable law.

In 1995, pursuant to the Ordinance and Bond Resolution, the City issued \$100.0 million in self-insurance bonds, and the proceeds were deposited in the Risk Management Fund to cover claim and lawsuit payments.

The Risk Management Fund revenues are premiums from the General Fund agencies and Detroit Department of Transportation (DDOT), earnings from the investment of fund assets, and reimbursements from the State. The amount of the annual claims premium is a five-year running average of actual payouts on damage claims and lawsuits. Claim and lawsuit payments of the General Fund agencies and DDOT are accounted for in the Risk Management Fund. The City also makes debt service payments on the related self-insurance bond issues.

Of the \$100.0 million self-insurance bonds issued in 1995, \$71.1 million were retired in previous years, leaving a balance of \$28.9 million of bonds payable at June 30, 2003. The bond principal was to be fully retired by fiscal year 2004-2005.

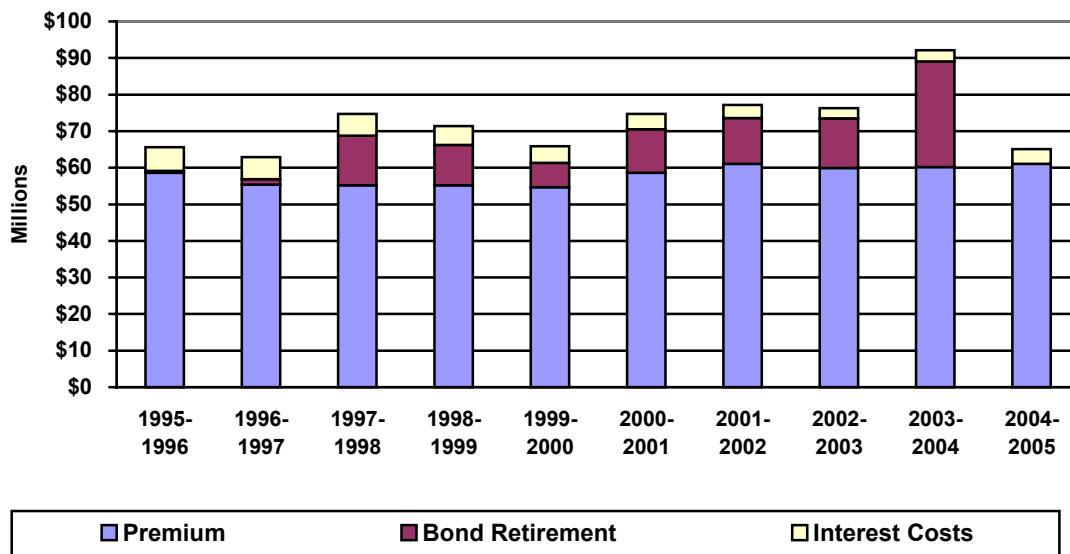
In 2003-2004, the City issued \$98.9 million in self-insurance bonds for the Risk Management Fund. The issue included the 2003-2004 Risk Management Claims Premium of \$60.2 million and refinanced the \$28.9 million balance of the original issuance. Financing the claims premium with long-term debt was to be a one-time occurrence, according to the Mayor's 2003-2004 Budget address.

The Mayor's Proposed Budget for fiscal year 2004-2005 includes a provision to issue an additional \$61.1 million in self-insurance bonds to "fund a Risk Management Fund payment". This year, like last, the Mayor is proposing to issue bonds to cover the annual premium amount for claims and litigation. The effect of doing so is to finance current year expenditures with long term financing.

The table on the following page shows the City's budget for each of the ten fiscal years, from 1995-1996 to 2004-2005, for premiums for claims and lawsuits against the City related to General Fund agencies and DDOT. In addition, the total appropriation includes debt service (bond principal and interest) on the self-insurance bonds.

Fiscal Year	Budgeted Appropriations (In Millions)						
	Premiums			Debt Service			Total Budgeted Appropriations
	General Fund	DDOT	Total Premiums	Net Bond Retirements	Bond & Interest Costs	Total Debt Service	
1995-1996	\$ 47.1	\$ 11.5	\$ 58.6	\$ 0.5	\$ 6.5	\$ 7.0	\$ 65.6
1996-1997	45.0	10.4	55.4	1.5	6.0	7.5	62.9
1997-1998	45.2	10.0	55.2	13.6	5.9	19.5	74.7
1998-1999	45.7	9.5	55.2	11.0	5.2	16.2	71.4
1999-2000	45.4	9.3	54.7	6.6	4.6	11.2	65.9
2000-2001	46.6	12.0	58.6	11.9	4.2	16.1	74.7
2001-2002	48.6	12.5	61.1	12.5	3.6	16.1	77.2
2002-2003	47.9	12.0	59.9	13.6	2.8	16.4	76.3
2003-2004 ¹	46.3	13.9	60.2	28.9	3.0	31.9	92.1
2004-2005	47.3	13.8	61.1	0.0	4.0	4.0	65.1
Ten Year Total	<u>\$ 465.1</u>	<u>\$ 114.9</u>	<u>\$ 580.0</u>	<u>\$100.1</u>	<u>\$ 45.8</u>	<u>\$ 145.9</u>	<u>\$ 725.9</u>

As shown in the table above, over the past ten years, the total Risk Management Fund appropriations for both premiums and debt service have ranged from a low of \$62.9 million in fiscal year 1996-1997 to a high of \$92.1 million in fiscal year 2003-2004. The fiscal year 2003-2004 appropriation included the retirement of the 1995 self-insurance bond issue that was rolled into the 2003 bond issuance. Debt service has added \$145.9 million to the risk management payments over the past ten years, an average of \$14.6 million per year. The average budgeted claims premium payment was \$58.0 million during this ten-year period. The following chart illustrates the additional cost the City has incurred due to the debt service on the self-insurance bonds.



¹ The Net Bond Requirement and Bond & Interest Cost for fiscal year 2003-2004 have been restated from the amounts shown in the Office of the Auditor General's 2003-2004 Budget Analysis from \$14.0 million and \$1.9 million, to \$28.9 million and \$3.0 million, respectively. The restatement is due to the early retirement of the 1995 self-insurance bonds.

The 2004-2005 proposed budget includes the claims premium and minimal interest, as the 2003 self-insurance issue has interest-only payments for the first two years. Principal payments on the self-insurance bonds issued in fiscal year 2003-2004 will commence during fiscal year 2005-2006. Consequently the City will have higher debt service payments from fiscal year 2005-2006 until the bonds mature in fiscal year 2012-2013.

The following table shows the actual expenditures, revenues, excess or deficiency of revenues, and fund balance of the Risk Management Fund for fiscal years 1994-1995 through 2002-2003 (the most recently completed fiscal year). Revenues include claims premiums made from the General Fund and DDOT. Expenditures are the amount paid out on claims and judgments during the year.

Actual Expenditures, Revenues, and Fund Balance (In Millions)				
Fiscal Year	<u>Revenues</u>	<u>Claims Expenditures</u>	Excess/ (Deficiency) of <u>Revenues</u>	<u>Fund Balance</u>
Beginning Balance				\$100.0
1994-1995	\$ 11.3	\$ 48.8	\$ (37.5)	62.5
1995-1996	56.9	57.8	(0.9)	61.6
1996-1997	59.2	52.8	6.4	68.0
1997-1998	50.0	55.6	(5.6)	62.4
1998-1999	53.2	74.0	(20.8)	41.6
1999-2000	56.3	61.8	(5.5)	36.1
2000-2001	60.4	51.7	8.7	44.8
2001-2002	60.9	54.0	6.9	51.7
2002-2003	<u>59.0</u>	<u>60.3</u>	<u>(1.3)</u>	50.4
Total	<u>\$467.2</u>	<u>\$516.8</u>	<u>\$ (49.6)</u>	

The balance of the Risk Management Fund was \$50.4 million on June 30, 2003. Over the nine-year period ended June 30, 2003, a total of \$516.8 million was paid for claims and lawsuits from the Risk Management Fund. These payouts were financed by \$467.2 million in revenues (primarily General Fund and DDOT claims premiums), and \$49.6 million of self-insurance bond proceeds.

Based on our analysis of the Risk Management Fund, we note these financial concerns:

- The estimated total liabilities of the Risk Management Fund included in the June 30, 2003 Comprehensive Annual Financial Report was \$178.8 million. The current portion of this liability, payable within one year, was estimated at \$8.4 million, while the long-term portion of the liability was estimated at \$170.4 million. The total liability of \$178.8 reflects a decrease of \$25.1 million from the prior year estimate of \$203.9 million. The average estimated total liability of the Risk Management Fund over the past nine years is \$188.9 million. While the total liability has decreased, the continued high estimated liabilities indicate that the City has not been able to adequately identify and address the causes of damage, liability and workers' compensation claims against the City.
- The balance of the 2003 self-insurance bond issue is now \$98.9 million. The \$61.1 million of additional bonds to be issued in fiscal year 2004-2005 will increase the self-insurance bond balance to \$160.0 million and will increase Risk Management related costs, specifically debt service payments, in future years. Any gains that the City makes

in reducing its day-to-day risk management claims will be masked, due to high and extended debt service payments for the new self-insurance bond issue, until the new bond issue is paid off. The estimated annual average cost of debt service on the 2003 bond issue is \$12.7 million per year, over ten years. The financing details of the fiscal 2004-2005 bond issuance have not been finalized.

DEPARTMENT OF TRANSPORTATION

The following schedule compares the 2004-2005 Mayor's Proposed Budget appropriations and revenues for the Detroit Department of Transportation (DDOT) operations, including the Detroit Transportation Corporation (DTC - "People Mover"), to the fiscal year 2003-2004 Budget:

	<u>In Millions</u>		
	<u>2004-2005 Mayor's Proposed Budget</u>	<u>2003-2004 Budget</u>	<u>Increase (Decrease)</u>
<u>Appropriations:</u>			
DDOT Operations	\$ 148.8	\$ 149.7	\$ (0.9)
DTC Support	7.7	10.3	(2.6)
Claims Fund	<u>14.7</u>	<u>14.3</u>	<u>0.4</u>
Total Appropriations	<u>\$ 171.2</u>	<u>\$ 174.3</u>	<u>\$ (3.1)</u>
<u>Revenues:</u>			
State Operating Assistance	\$ 58.1	\$ 57.9	\$ 0.2
Farebox Revenue	29.1	31.2	(2.1)
General Fund Contribution to DDOT	69.6	68.2	1.4
General Fund Contribution to DTC	7.7	10.3	(2.6)
Other Operating Revenue	0.9	0.8	0.1
Claims Fund Revenue	<u>5.8</u>	<u>5.9</u>	<u>(0.1)</u>
Total Revenues	<u>\$ 171.2</u>	<u>\$ 174.3</u>	<u>\$ (3.1)</u>

As reflected in the schedule, the 2004-2005 Mayor's Proposed Budget is quite comparable to the 2003-2004 Budget.

State Operating Assistance

Public Act 51 of 1951 restricts State Operating Assistance for urban public transit agencies, with a population greater than 100,000, to an amount up to 50% of their eligible operating expenses, as defined by the State of Michigan Department of Transportation. An eligible expense reimbursement formula is used to compute the amount of operating assistance that urban transit agencies receive from the State. An adjusted amount of eligible expenses is multiplied by a percentage, determined by the State, to calculate the amount of the distribution to transit agencies. According to the formula, the DDOT receives 65% and the Suburban Mobility Authority for Regional Transportation (SMART) receives 35% of the total distribution amount allocated to the urban agencies. Michigan Department of Transportation documents show, for State fiscal year 2004, October through September, that State Operating Assistance will cover \$55.7 million of DDOT's \$163.8 million Eligible Operating Expenses and the remaining \$108.1 million is the Local Share, to be covered through DDOT revenues and the General Fund Subsidy.

The 2004-2005 Mayor's Proposed Budget includes an estimate of \$58.1 million for State Operating Assistance, a \$ 0.2 million increase from the previous budget. State Operating

Assistance supports approximately 34% of DDOT's budgeted operating expenditures. The DDOT estimate for fiscal year 2004-2005 may be slightly overstated.

Farebox Revenue

Budgeted farebox revenue is approximately \$29.1 million for fiscal year 2004-2005, a decrease of approximately \$2.1 million or 6.7% from fiscal year 2003-2004. DDOT actual operating revenues, including farebox revenue, was \$25.2 million in fiscal year 2002-2003, a \$1.1 million increase from fiscal year 2001-2002. The Mayor's 2004-2005 Proposed Budget includes an additional \$2.0 million in farebox revenue based on the anticipated revenue from a new \$ 0.75 charge to disabled persons riding the buses. In the past, it was believed that fare increases should result in more revenue. However, it has been noted that fare increases have discouraged ridership and revenue has not increased as anticipated.

In our opinion, the farebox revenue in the 2004-2005 Mayor's Proposed Budget appears overly optimistic based on past history at DDOT. According to the City's financial system, farebox revenues for the nine months ended March 31, 2004 total approximately \$15.9 million, which equals the approximate \$15.9 million for the nine months ended March 31, 2003. Actual operating revenues, including farebox revenue, for fiscal year 2002-2003 was \$25.2 million. At the current rate, it is unlikely that DDOT will achieve last year's revenue levels or its budgeted revenue of \$31.2 million for fiscal year 2003-2004. Unless dramatic efforts are undertaken to increase ridership, it is unlikely that DDOT's farebox revenues will grow to the level budgeted for fiscal year 2004-2005.

General Fund Contribution - DDOT

The budgeted General Fund Contribution (Subsidy) to DDOT is \$69.6 million for fiscal year 2004-2005. This General Fund contribution to DDOT represents a \$1.4 million, or 2.1%, increase from the previous year's budgeted amount of \$68.2 million. The 2004-2005 General Fund Subsidy has increased 2.1% from the previous year despite a decrease in appropriations from fiscal year 2003-2004.

Proposed Layoffs

There are 112 employees in DDOT's maintenance division who are included in the Mayor's layoffs for fiscal year 2004-2005.

Vacant Position Changes

The 2004-2005 Mayor's Proposed Budget eliminates a net of eight positions. The eight positions are comprised of 14 positions (includes six auto repair sub-foremen) netted against 22 vacant positions (six coach service attendants, five general auto body mechanics, three auto mechanics, three general auto mechanics, and other non-mechanic positions).

Employee Turnover Savings

Employee Turnover Savings is the amount expected to be saved due to temporarily vacant positions. There are no Employee Turnover Savings for DDOT included in the 2004-2005 Mayor's Proposed Budget. The amount that was budgeted for Employee Turnover Savings in the prior fiscal year 2003-2004 Budget was approximately \$3.9 million for DDOT operator and mechanic positions.

Overtime

The amount of overtime that is included in the 2004-2005 Mayor's Proposed Budget is \$12.7 million compared to \$17.6 million budgeted in fiscal year 2003-2004, a decrease of \$4.9 million or 27.8%. DDOT actual overtime for 2002-2003 and 2001-2002, per the City's Brass reports, totaled \$21.0 million and \$19.9 million respectively.

Net Operating Losses

The pattern of the DDOT's net operating losses is well documented, as are the public policy reasons underlying continued subsidies to transit operations. The following schedule details the DDOT actual and expected net operating losses over recent years. The data for this schedule was obtained from the City's Comprehensive Annual Financial Report (CAFR) for fiscal years ended June 30, 1999 through June 30, 2003, Budget Department data for fiscal year ending June 30, 2004, and the Mayor's Proposed Budget for 2004-2005.

Period	In Millions			
	Operating Revenue (A)	Operating Expense (B)	Net Operating (Loss)	Transfers from the General Fund
1998-1999	\$ 31.4	\$ 160.6	\$ (129.2)	\$ 51.0
1999-2000	29.0	172.6	(143.6)	60.2
2000-2001	25.1	187.1	(162.0)	74.2
2001-2002	24.1	187.4	(163.3)	79.4
2002-2003	25.2	196.2	(171.0)	75.5
2003-2004 (C)	32.1	164.0	(131.9)	78.5
2004-2005 (D)	29.9	163.5	(133.6)	77.3

(A) Operating revenue consists primarily of farebox revenue.

(B) Budgeted operating expenses do not include the General Fund contribution for operation of the People Mover, and the Capital Improvement Bonds in 2002-2003 and 2003-2004.

(C) Estimated

(D) Proposed

The above schedule clearly shows a trend of declining operating revenue and increasing operating expenses over the past five fiscal years, for which actual data is available. Large net operating losses are also expected in the 2003-2004 and 2004-2005 fiscal years.

Conclusion

Based on our analysis, the budgeted revenues and appropriations included in the 2004-2005 Mayor's Proposed Budget for DDOT are not reasonable. Farebox revenues and State Operating Assistance are overstated. Operating expenses are understated based on past history.

DETROIT TRANSPORTATION CORPORATION
(PEOPLE MOVER)

For fiscal year 2004-2005, the City has budgeted \$7.7 million to the Detroit Transportation Corporation (DTC), in the form of a General Fund Subsidy. The detailed budget for the DTC is not incorporated in the City's budget. The following schedule compares the DTC summary budget for fiscal years 2004-2005 and 2003-2004. The budget figures were provided to us by DTC.

	Millions		
	Budget		Increase/
	<u>2004-2005</u>	<u>2003-2004</u>	<u>(Decrease)</u>
<u>Revenues:</u>			
Operating Revenue:			
Fare Gate Revenue	\$ 0.4	\$ 0.2	\$ 0.2
Pass Sales & Token Sales	<u>0.4</u>	<u>0.3</u>	<u>0.1</u>
Total Operating Revenue	\$ 0.8	\$ 0.5	\$ 0.3
Non-Operating Revenue:			
FTA Grant Revenue	\$ 2.8	\$ 2.1	\$ 0.7
CMAQ Grant Revenue	-	0.4	(0.4)
DDA Bond Revenue	0.8	-	0.8
Miscellaneous	<u>0.6</u>	<u>0.8</u>	<u>(0.2)</u>
Total Non-Operating Revenue	\$ 4.2	\$ 3.3	\$ 0.9
Total Revenues	\$ 5.0	\$ 3.8	\$ 1.2
<u>Expenses:</u>			
Operating Expenses:			
Salaries & Benefits	\$ 7.5	\$ 7.4	\$ 0.1
Maintenance & Renovation	1.5	2.6	(1.1)
Other Operating Expenses	<u>3.1</u>	<u>3.4</u>	<u>(0.3)</u>
Total Operating Expenses	\$ 12.1	\$ 13.4	\$ (1.3)
Other Expenses	<u>0.6</u>	<u>0.6</u>	<u>0.0</u>
Total Expenses	\$ 12.7	\$ 14.0	\$ (1.3)
City Subsidy	<u>\$ 7.7</u>	<u>\$ 10.2</u>	<u>\$ (2.5)</u>

The \$7.7 million subsidy in the 2004-2005 Mayor's Proposed Budget represents 60.6% of the total funding necessary to operate the People Mover, compared to 73.0% in the prior year. Changes in budgeted Revenues and Expenditures are detailed on the next page.

Faregate Collections, Pass and Token Sales

There is an expected \$0.3 million increase in faregate revenue due to the completion of the reconstruction portion of the RenCen project. Full time operation of the People Mover is due to resume sometime in May of 2004.

DDA Bond Revenue

The DTC expects to receive \$0.8 million in Bond Revenue from the Downtown Development Authority in fiscal year 2004-2005. The funds will be received directly by the DTC, and will not pass through the Detroit Department of Transportation (DDOT).

Expected Federal Transit Administration (FTA) Grant

The FTA Grant is expected to increase from \$2.1 million to \$2.8 million, an increase of \$0.7 million, due to the transfer of a grant from DDOT to DTC. According to DTC, these additional grant funds had been earmarked for DDOT's Vintage Trolley project. The DDOT was about to lose the grant funds because it was not ready to proceed with the project. The DTC is currently prepared for a rail modernization project, which is acceptable under this portion of the FTA grant. The DTC expects to receive the grant previously slated for the DDOT. Without the additional funds for the rail modernization, the annual FTA Grant received by the DTC is between \$0.6 and \$0.7 million.

Maintenance and Renovation

Budgeted Facility Maintenance and Contract Services will decrease by \$1.1 million, due primarily to the reduction of the City's subsidy, and the shifting of budgeted funds from maintenance to capital spending.

DTC Subsidy

The DTC is primarily funded by grants from the City. The budgeted subsidy to the DTC is \$7.7 million for 2004-2005, a decrease of \$2.5 million from the 2003-2004 budget. Based upon the estimated ridership of 1,550,000, the cost of the budgeted subsidy is \$4.99 for each \$0.50 ride.

Although the \$2.5 million reduction in the subsidy represents 18% of DTC's 2003-2004 expenditures of \$14.0 million, the Mayor stated in his 2004-2005 Budget Message that the General Fund subsidy reduction would have no impact upon DTC's operations. This reduction may well have no impact upon DTC's operations in 2004-2005, however, the reduction of maintenance and renovation may have negative effects in the long run.